

STATE OF NEW YORK

DIVISION OF TAX APPEALS

In the Matter of the Petition	:	
of	:	
CERTIFIED HEATING OILS, INC.	:	:DETERMINATION
for a Hearing with Regard to a Bond Required	:	
under Section 283 of Article 12-A of the	:	
Tax Law.	:	

Petitioner, Certified Heating Oils, Inc., 93 Wright Avenue, Staten Island, New York 10303, filed a petition for a hearing with regard to a bond required under section 283 of Article 12-A of the Tax Law (File No. 807944).

A hearing was held before Catherine M. Bennett, Administrative Law Judge, at the offices of the Division of Tax Appeals, Riverfront Professional Tower, 500 Federal Street, Troy, New York, on April 25, 1990 at 1:15 P.M., with all briefs to be submitted by May 22, 1990. Petitioner appeared by DeGraff, Foy, Conway, Holt-Harris & Mealey, Esqs. (James H. Tully, Jr., Esq., of counsel). The Division of Taxation appeared by William F. Collins, Esq. (Carroll R. Jenkins, Esq., of counsel).

ISSUE

Whether the Division of Taxation properly determined that petitioner must file a surety bond in the amount of \$439,000.00, increased from \$186,000.00, as a condition of maintaining its registration as a New York State motor fuel distributor.

FINDINGS OF FACT

Petitioner, Certified Heating Oils, Inc., is engaged in the distribution of gasoline and home heating fuel and has been operating as a fuel distribution business since 1946.

Petitioner is registered with the New York State Department of Taxation and Finance as a motor fuel distributor pursuant to section 283 of Article 12-A of the Tax Law and part 411 of the regulations.

By a Notice of Cancellation or Termination dated February 5, 1990, the Fireman's Fund Insurance Company notified the New York State Department of Taxation and Finance that a surety bond covering Certified Heating Oils, Inc. in the amount of \$186,000.00 would be cancelled and/or terminated effective March 6, 1990.

On or about February 23, 1990, the Division of Taxation requested from Certified Heating Oils, Inc. a copy of petitioner's certified financial statement. The Division received the compiled financial statements of both Certified Heating Oils, Inc. and Joseph Marino, its president. These compiled statements are not "certified financial statements pursuant to an audit" but are rather statements prepared from information that is the representation of management.

In a letter dated March 6, 1990, Certified Heating Oils, Inc. and its president, Joseph J. Marino, were informed that the Division of Taxation had reviewed the amount of the surety bond required to be filed. The correspondence indicated that a replacement security in the amount of \$439,000.00 was being required and that either a surety bond or other acceptable collateral must be filed according to the regulations within 30 days of March 6. Petitioner was also apprised of its right to protest this decision within seven days by written petition.

The Division of Tax Appeals received the petition of Certified Heating Oils, Inc. on March 20, 1990.

A hearing was scheduled for Tuesday, April 3, 1990 for the purpose of determining the same issue herein. At that time, petitioner requested an opportunity to post a bond or other security in the amount of \$186,000.00, the amount of surety bond that had recently been cancelled, with an opportunity to pursue the additional \$250,000.00 necessary to post the new bond being requested by the Division of Taxation. The case was then rescheduled to be heard on April 25, 1990 for the purpose of determining whether the preliminary bond of \$186,000.00¹ should be increased to \$439,000.00.

¹Periodically during the hearing, this amount (\$186,000.00) was also referred to as \$189,000.00.

On April 13, 1990, the Division of Taxation issued a Notice of Suspension of Motor Fuel Registration under Article 12-A of the Tax Law to Certified Heating Oils, Inc. since it was unable to submit the security amount of \$186,000.00.

On or about April 20, 1990, the Division of Taxation confirmed receipt and acceptance of a letter of credit from the Community National Bank & Trust Company of New York in the amount of \$189,000.00 on behalf of Certified Heating Oils, Inc. upon which the Division acted to withdraw the suspension of petitioner's registration as a motor fuel distributor.

Certified Heating Oils, Inc. remained under obligation to file an additional bond of \$250,000.00 until final disposition of this matter at the April 25, 1990 hearing since petitioner did not submit additional security before this proceeding. The registration was suspended effective midnight April 24, 1990. The Administrative Law Judge ordered the Division of Taxation to lift the suspension of the registration pending the outcome of this determination.

The Division of Taxation presented as its witness, Jack Butler, a supervisor of the Motor Fuel Bond Unit. Mr. Butler was responsible for review of petitioner's file to make a determination as to whether the security which the Division was holding was sufficient or whether it should be revised in some way. Mr. Butler testified that he received a computer printout showing the number of gallons of gasoline involved in transactions by Certified Heating Oils, Inc. for the past six months. The number of gallons of motor fuel expected to be imported into this State, sold, transferred or otherwise distributed within New York State is the amount of gallonage that is used in a computation indicating the potential future tax liability of the company.

Mr. Butler further testified that other factors considered included the availability of a current certified financial statement, the filing history of the company, any outstanding liabilities or current balance owed by the company.

The computation performed by Mr. Butler with respect to the gallonage for a six-month period led him to conclude that the six-month activity of Certified Heating Oils, Inc. involved

3,026,823 gallons of motor fuel. This was multiplied by 14.5¢ sales and motor fuel tax combined rates, resulting in a potential six-month liability of \$438,889.34. For the purpose of revising the surety bond, petitioner was notified that the new bond requirement would be raised to \$439,000.00.

Joseph Marino, president of Certified Heating Oils, Inc., testified that when he received the information with respect to the increase of the surety bond amount from \$186,000.00 to \$439,000.00, he immediately contacted his insurance broker requesting replacement of the bond at the newly determined amount. Introduced into evidence was a letter from Countrywide Facilities Corporation, the insurance broker who attempted to obtain a bond by contacting eight different companies on behalf of petitioner. At least half of these companies indicated they would not write such insurance and several others indicated they would consider writing such a bond only with full collateral in the form of a letter of credit or cash. The Countrywide correspondence stated that many of the bonding companies are now cancelling these bonds industry-wide as a matter of course and those who are still willing to write such bonds have now imposed "collateral requirements and premiums [which] have become outrageous."

Petitioner further presented correspondence dated April 24, 1990 from Community National Bank & Trust Company of New York indicating that the bank was in the process of considering a request from Certified Heating Oils, Inc. for a letter of credit in the amount of \$250,000.00. Mr. Marino testified that the basis for the line of credit was to be the equity in the commercial building at which Certified Heating Oils was located. This building is owned personally by the president of the company, Joseph Marino.

Mr. Marino testified that his expectation of sales of fuel will be approximately 25% less in the first six months of 1990 than in the last six months of 1989, the months upon which the computation by Mr. Butler was made. However, no evidence was offered to prove such decline during those months in 1990 which preceded this hearing.

It has been stated by both parties and agreed that petitioner's filing history has been commendable and its compliance without blemish.

SUMMARY OF THE PARTIES' POSITIONS

Petitioner takes exception to the Division of Taxation's calculation of the increased bond amount on the basis that the Division of Taxation based the new bond amount solely on petitioner's estimated six-month potential tax liability. Petitioner rejects this since it claims that its excellent record of compliance was not taken into consideration and that, as a result, the Division of Taxation set a bond which was arbitrary and capricious, and that the conduct by the Division was an abuse of discretion.

The Division of Taxation asserts that as a motor fuel distributor, pursuant to the Tax Law, petitioner must maintain adequate security as defined by the law and applicable regulations. The Division further reiterates a point raised at hearing with respect to the use of uncertified financial statements as well as the fact that a personal financial statement cannot take the place of the corporate financial statement when in fact it is the corporation which is the applicant for registration and the distributor of the motor fuel.

CONCLUSIONS OF LAW

A. Tax Law § 283(3) provides, in part:

"The tax commission shall require a distributor to file with the department of taxation and finance a bond issued by a surety company approved by the superintendent of insurance as to solvency and responsibility and authorized to transact business in this state or other security acceptable to the tax commission, in such amount as the tax commission may fix, in an amount determined in accordance with rules and regulations prescribed by it, to secure the payment of any sums due from such distributor (i) pursuant to this article and (ii) pursuant to articles twenty-eight and twenty-nine of this chapter with respect to sales and uses of motor fuel. The tax commission shall require that such a bond or other security be filed before a distributor is registered, and the amount thereof may be increased at any time when in its judgment the same is necessary as a protection to the revenues under this article and articles twenty-eight and twenty-nine...."

B. The foregoing function of the Tax Commission was transferred to the Commissioner of Taxation and Finance by section 14 of chapter 282 of the Laws of 1986.

C. The purpose of Tax Law § 283(3) is to protect the revenues of New York State by requiring the registration of distributors and the filing by such distributors of a bond or other security to secure the payment of motor fuel and sales and use taxes (see, Matter of Major Oils, Tax Appeals Tribunal, August 4, 1988). The Division of Taxation adopted regulations pursuant

to Tax Law § 283 which describe the information that a person must submit to the Division of Taxation before it may be registered as a distributor of motor fuel as well as providing the method by which the bond or other security is determined (see, 20 NYCRR part 411).

D. 20 NYCRR 411.1(b) requires the following:

"Before any person may be registered as a distributor of motor fuel, such person must submit to the department:

(1) a completed application for registration as a distributor of motor fuel (form TP-128.3);

(2) current unqualified financial statements certified by a certified public accountant pursuant to an audit conducted by such accountant; and

(3) an estimate of the monthly number of gallons of motor fuel expected to be:

(i) imported or caused to be imported into the State for use, distribution, storage or sale within the State;

(ii) produced, refined, manufactured or compounded within the State; and

(iii) sold, transferred, used or otherwise distributed within the State."

E. Regulation 20 NYCRR 411.1(c) provides, in pertinent part, that:

"The department (in order to protect article 12-A-revenues and articles 28 and 29-revenues with respect to motor fuel) will periodically review the financial status of registered distributors and may, at any time subsequent to registration of any person as a distributor, require any such distributor to submit to the department:

* * *

(2) current unqualified financial statements certified by a certified public accountant pursuant to an audit conducted by such accountant."

Subdivision (d)(2) of the same section provides that if that distributor fails to supply such current unqualified financial statements, the distributor's registration will be cancelled. If the requirement to supply such statements is waived, then the distributor can be required to file a bond or other acceptable security deemed appropriate by the Division regardless of the distributor's financial status.

F. Pursuant to Tax Law § 283(3), the regulations at 20 NYCRR 411.2(b)(1) entitled "Determination of the amount of a bond" provide, in relevant part, that:

"Prior to the approval of an application for registration as a distributor of motor fuel and during any subsequent review of a registered distributor, the Department of Taxation and Finance, in determining the amount or sufficiency of a bond, will:

- (i) determine the estimated or representative six-month maximum potential tax liability of the applicant or of the distributor (see paragraph [2] of this subdivision);
- (ii) analyze the certified financial statements of the applicant or distributor with particular emphasis on the ratio of current assets to current liabilities and net worth (total assets less total liabilities) as determined in accordance with generally accepted accounting principals;
- (iii) evaluate any independent information concerning an applicant's or distributor's nature of operations, reliability, overall financial status, liquidity, or history of financial solvency and stability; and
- (iv) review the taxpayer's compliance record to determine whether there are or were any delinquencies in filing returns and/or payment of taxes as a distributor of motor fuel or for any other taxes due New York State for which the applicant or distributor may be or may have been responsible."

Paragraph (2) of this subdivision indicates that the maximum potential tax liability is determined based on an anticipated number of gallons of motor fuel expected to be sold or otherwise distributed within New York State during a representative six-month period. The number of gallons of motor fuel determined for such representative six-month period is then multiplied by the rate of motor fuel tax per gallon and by the applicable tax rate of the prepaid sales tax per gallon. In this case, the combined motor fuel tax and prepaid sales tax was indicated to be 14.5¢ per gallon.

G. In this case, petitioner has not submitted, as required, an unqualified financial statement certified by a certified public accountant pursuant to an audit by such accountant. In Matter of Benak Corporation (State Tax Commission, January 15, 1985) the State Tax Commission noted that "[t]he purpose of this requirement is to provide independent verification of the reliability of a distributor's financial statements and, in turn, its financial condition." Since petitioner did not submit the required statements, the Division of Taxation could have cancelled petitioner's registration; however, in the alternative, it chose to review its filing history, compliance record and overall reliability, as well as compute a bond based on six months' potential tax liability. In the computer printouts submitted by the Division of Taxation,

the gallonage for a period of 20 months totalled 9,162,122 gallons which, when reduced to a six-month average representative period, would have resulted in the requirement of approximately a \$400,000.00 bond. If one refers to the 12 months of gallonage encompassing the calendar year 1989, the bond requirement would result in an amount just over \$441,000.00. From the information submitted with respect to the gallonage, petitioner's business seemed to be on a steady upward pace. Thus, the calculation based on the six months between July 1989 and December 1989 appears to be a representative six-month period with respect to petitioner's business.

H. In reviewing the information and factors that the Division of Taxation must consider in the determination of a new bond amount set forth by the regulations described above, the Division of Taxation essentially did not perform an analysis of the compiled financial statements that were submitted by petitioner since it is clear by regulation that the financial statements can only be deemed reliable and be analyzed for this purpose if they are "certified pursuant to an audit by a certified public accountant," which these were not. Since the certification of such statements gives some assurance of validity, the questionable reliability that one can place on compiled statements in a situation like the one at hand renders any analysis of the financial data virtually meaningless. Furthermore, the Division of Taxation performed an evaluation of other independent information with respect to the nature of operations, overall financial status and review of petitioner's compliance record. The Division of Taxation's actions and computation with respect to an increase in the bond amount appears to be in complete accord with the statute and regulations.

I. Petitioner's assertion that the Division of Taxation has exercised an abuse of discretion is without merit. In essence, the application of the regulations as they stand with respect to the issuance and determination of bond requirements leave little discretion to the Division at all. With respect to the contention that the bond is excessive, petitioner could have submitted information showing that the calculation should be revised in some way. Further, petitioner was given an opportunity to submit certified financial statements. Although having to bear the

financial cost of doing so, such submission may have resulted in an alternative arrangement.

J. The petition of Certified Heating Oils, Inc. is hereby denied and the bond requirement of \$439,000.00 is sustained.

DATED: Troy, New York

ADMINISTRATIVE LAW JUDGE